85-1273

No. ...-...

Supreme Court, U.S.
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In the Supreme Court

OF THE

United States

OCTOBER TERM, 1985

ALEXANDER F. EAGLE,
Petitioner,

VS.

AMERICAN TELEPHONE AND TELEGRAPH COMPANY,
a Corporation,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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QUESTIONS PRESENTED

1. A complaint of the sole plaintiff* in a state court asserts his claim for less than the $10,000 federal diversity jurisdictional minimum and seeks class action status for all minority shareholders of a corporation. Aggregation of like claims of minority shareholders would exceed the jurisdictional minimum, and aggregation would be permissible *if* the claims were merely derivative of a claim by the corporation. But plaintiff asserts as *his* theory of recovery one on which aggregation is not permissible under *Snyder v. Harris*, 394 U.S. 322 (1969). Is not plaintiff the "master of the case" he seeks to present, so that a federal court, after removal, may not give a different characterization to plaintiff's claim in order to retain jurisdiction, and must it not remand, leaving plaintiff to risk that the state courts may hold that state law does recognize a cause of action such as plaintiff claims?

2. A second question is present if federal jurisdiction is upheld. After denying remand, the federal court granted a summary judgment of dismissal of the case, not on the basis that there was no appropriate relief if plaintiff should prove the case alleged in his complaint, nor on the basis that stipulated and undisputed facts required dismissal, nor on the basis that any pretrial order formulated the issues so as to exclude the theory on which relief was available, but on the basis that plaintiff's counsel during pretrial had expressed as his theory of relief one in which there were no damages. Was that not a misuse of pretrial procedure, in that the rule of pleading, that a plaintiff should be entitled to whatever relief the facts warrant, is equally applicable to pretrial practice?

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*The caption contains the names of all parties in the court below.

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VS.

AMERICAN TELEPHONE AND TELEGRAPH COMPANY,
a Corporation,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

The petitioner, Alexander F. Eagle, prays that a writ of certiorari issue to review the judgment of the Court of Appeals for the Ninth Circuit in its case No. 84-1636 entitled *"Alexander F. Eagle, Plaintiff-Appellant vs. American Telephone and Telegraph Company, a Corporation, Defendant-Appellee"*.

OPINIONS BELOW

The opinion of the Court of Appeal is reported at 769 F.2d 541 and is in Appendix A. The opinion of the District Court is not reported but it is in Appendix C.

JURISDICTION

The Court of Appeals had jurisdiction under 28 U.S.C. § 1291. Its judgment was entered on August 19, 1985, and a timely

petition for rehearing, filed on August 29, 1985, was denied on October 30, 1985. (App. p. 13a) This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

The first issue presented by this petition is whether the District Court had jurisdiction at all.

STATUTES INVOLVED

28 U.S.C. § 1332 provides:

> "(a) The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of $10,000, exclusive of interest and costs, and is between —
>
> (1) citizens of different States . . . ."

28 U.S.C. § 1441 provides:

> "(a) Except as otherwise expressly provided by Act of Congress, any civil action brought in a State court of which the district courts of the United States have original jurisdiction, may be removed by the defendant or the defendants, to the district court of the United States for the district and division embracing the place where such action is pending."

STATEMENT OF THE CASE[1]

This case is another example of intrusion by federal courts on cases properly belonging to a state court and involving only questions of state law.

Prior to the recent antitrust restructuring of the Bell system, telephone service in California was provided by Pacific Telephone & Telegraph Company (hereafter "Pacific"), regulated by the California Public Utility Commission. Before October, 1981, respondent American Telephone and Telegraph Company (hereafter "AT&T") owned 90% of Pacific's capital stock. The shares comprising the other 10% were owned by numerous others, one of

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[1]All facts in this statement are taken from the opinions of the two courts below.

whom is petitioner Eagle. As the 90% controlling stockholder of Pacific, AT&T had power under California law to force a merger of Pacific into a wholly-owned subsidiary of AT&T, and in October, 1981, did so. Thereby Pacific's minority stockholders were forced to part with their shares.

The Internal Revenue Code permitted telephone companies to take accelerated depreciation. As claimed by plaintiff, for reasons of its own AT&T did not wish its subsidiaries in the Bell system to do so, and, at AT&T's command, Pacific did not. In proceedings beginning in the California Public Utility Commission and carried into the California Supreme Court, it was held that Pacific acted imprudently in not taking the accelerated depreciation. Had it done so, Pacific's federal income taxes would have been much less, and accordingly its rate base and the rates payable and paid by telephone users would have been less. Pacific was therefore ordered to refund to the rate-payers the difference between what they paid and what they would have paid if the accelerated depreciation had been taken and lower taxes thus incurred. Despite these rulings Pacific, on the command of AT&T, obstinately continued to refuse to take accelerated depreciation. By amendment in 1969 to Section 167 of the Internal Revenue Code, utilities were denied the right to take accelerated depreciation if the benefit was to "flow through" to the rate-payers and not retained to increase investment in plant and equipment, unless the utility had theretofore been taking accelerated depreciation. The consequence was that Pacific could not diminish its taxes but yet had to fix its rates and make refunds as if it were diminishing taxes.

The California Supreme Court in *City and County of San Francisco v. Public Utilities Com.*, 6 Cal.3d 119, 98 Cal.Rptr. 286, 490 P.2d 798 (1971), agreed with the Public Utility Commission that "management's discretion has exceeded a reasonable and prudent course respecting income taxes to the detriment of the public interest and that it was fair and reasonable and in the public interest to compute Pacific's income tax expense . . . on the basis of the use of accelerated depreciation . . . ." (p. 127). The California Supreme Court held that Pacific's inability to switch to accelerated depreciation was "due to its original imprudent deter-

mination to pay federal income taxes on a straight line depreciation basis and its obstinacy . . . in adhering to the imprudent determination", that the effect of its refusal to switch and obstinacy "was to cast a significant burden on itself", and that it "in essence placed itself in the position of paying a large income tax bill, part of which was unnecessary and was not to be recovered in higher rates" (p. 128).

In consequence, at the time of the merger consummated in October, 1981, Pacific had on its books a federal tax liability of $1½ billion, although at the same time it had made $381 million of refunds to rate-payers as though it had diminished its tax liability and was required to charge rates calculated on what would be the rate base if lower taxes were paid and payable.

This was a debacle, and it was caused by AT&T's exercise of its power as Pacific's controlling stockholder. The huge tax liability diminished the value of Pacific's shares, and this suit was commenced against AT&T in September, 1981, in a California state court by Eagle, one of Pacific's minority stockholders.[2] Eagle asserted on his own behalf a claim of $4200, and the complaint sought class action status for all minority stockholders.

The case of *Jones v. Ahmanson & Co.*, 1 Cal.3d 93, 81 Cal.Rptr. 592, 460 P.2d 464 (per Chief Justice Traynor, 1969) was an epochal decision in California law; it established and expanded the fiduciary duty of a majority stockholder to minority stockholders. The basis of Eagle's claim was that AT&T had violated that fiduciary duty under the *Ahmanson* rule.

Before any class determination had been made, defendant AT&T removed the case to the United States District Court in San Francisco, purportedly under 28 U.S.C. § 1441(a). A motion to remand was denied. A petition to the Court of Appeals for a writ of mandamus to compel remand was denied because, "under the compulsion of *Ex Parte Harding*, 219 U.S. 363 (1911)", error

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[2]After the merger, legislation was obtained from Congress forgiving some of Pacific's tax liability.

in denying remand is not reviewable by mandamus but must await appeal from a final judgment.[3]

Thereafter, still with no determination that the action could proceed as a class action, the district court dismissed the action on AT&T's motion for summary judgment. It did so, not upon any determination respecting evidence, but on the basis that a remedy within the pleadings and the facts was precluded by pretrial proceedings.

The Court of Appeals affirmed the judgment.

REASONS FOR GRANTING THE WRIT

We submit two reasons for granting the writ.

I.

THE DISTRICT COURT HAD NO JURISDICTION. THE DECISIONS BELOW IGNORE THE BASIC RULE THAT THE PLAINTIFF IS THE MASTER OF THE CASE HE SEEKS TO PRESENT.

Once again it becomes necessary to remind the lower federal courts of the limits of their jurisdiction, to rein in their intrusion on the jurisdiction of state courts, and to respect the statutory limits on removal of cases involving no federal question but only diversity of citizenship, particularly in this age of over-burdened dockets and doubts of the wisdom of diversity jurisdiction. As said in *Snyder v. Harris*, 394 U.S. 322, 340 (1969), the policy of the statute on diversity jurisdiction calls for its strict construction.

Only by adding to Eagle's claim of $4200 the claims of others in the requested class of Pacific's minority stockholders could the necessary jurisdictional amount of $10,000 be reached. But in *Snyder v. Harris, supra*, this Court, facing that subject in class action context, held that separate claims of the various claimants

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[3]From this order of the Court of Appeals this Court denied a petition for a writ of certiorari, *Eagle v. United States District Court for the Northern District of California (American Telephone & Telegraph Company, Real Party in Interest)*, 459 U.S. 1071 (1982).

in a class action may not be added together to satisfy the jurisdictional requirement.

The court below reasoned that the claims of the minority shareholders were not separate but derivative in character, *i.e.*, that the suit was one to enforce a claim of Pacific against AT&T. But it is not for any federal court to decide whether the claim that the plaintiff seeks to present for decision is derivative or is one asserted by the stockholder as his individual claim against the defendant. As this Court has long and often taught, a plaintiff is the "master of his claim". That principle has a long history of application in litigation involving the jurisdiction of the federal courts over cases "arising under" the patent laws. *Luckett v. Delpark*, 270 U.S. 496 (1926) restated and reaffirmed the principle, dating back to *Wilson v. Sandford*, 51 U.S. (10 How.) 99 (1850), that whether a case is or is not within the jurisdiction of the federal courts depends on whether the plaintiff has *chosen* to base his claim upon state law or upon the patent laws. In *Luckett* this Court said that "the plaintiff is absolute master of what jurisdiction he will appeal to . . . ." (p. 508). So also, *Henry v. A.B. Dick Co.*, 224 U.S. 1 (1912) and *The Fair v. Kohler Die & S. Co.*, 228 U.S. 22, 25 (1913), where this Court said: "Of course, the party who brings a suit is master to decide what law he will rely upon . . . ." The rule has been applied by the Ninth Circuit in *Koratron Company v. Deering-Milliken, Inc.*, 418 F.2d 1314 (9 Cir. 1969), 10 A.L.R. Fed. 636, in which this Court denied *certiorari*, 398 U.S. 909. The rule that the plaintiff is master to choose what law he will rely upon has also been referred to in other kinds of cases involving the jurisdiction of federal courts; *e.g., Pan American P. Corp. v. Superior Court*, 366 U.S. 656 (1961); *Franchise Tax Bd. v. Laborers Vac. Trust*, 463 U.S. 1, 22 (1983).

Here plaintiff, Eagle, asserts that *under California law* he has an individual claim against AT&T for breach of its fiduciary duty as the majority shareholder to him as a minority shareholder, running directly from AT&T to him, and that he is *not* asserting a derivative claim belonging to Pacific. It will not do to contest or for the federal court to hold that no such claim exists. It *is* the claim which Eagle tendered to *a state court* for its determination.

Perhaps no such personal claim exists, and plaintiff takes the risk that it does not and that the state courts will accordingly dismiss his action.[4] But, whether it does or does not is a question of California law and is to be decided by the California courts. The court below thought the question was governed by a 1964 decision of an intermediate California appellate court, *O'Hare v. Marine Electric Co.*, 229 Cal.App.2d 33, 39 Cal.Rptr. 799. Plaintiff contends that it is governed by the later decision of a higher California court, its Supreme Court, in *Jones v. Ahmanson & Co., supra.* The court below notes that the "dividing line [between separate and distinct claims and derivative ones] is not clear" (App. 8a). Which view is correct, and where the line is to be drawn, are for the California courts to say. To use the language of the man on the street, the question is no business of the federal court.

The decision below presents both an anomaly and an absurdity. Having first held that the claim presented by Eagle is derivative, the court then held that no such claim exists, and therefore dismissed it. The court establishes its jurisdiction by first *creating* a claim and then *denies* its existence. It denies existence of the very foundation upon which, alone, it could have jurisdiction to act at all.

The gist of the first reason we present for granting the writ can be summed up simply: Eagle chose to present as his claim a supposed personal and not derivative claim. Therefore, the jurisdictional amount necessary to the removal was absent. Whether the kind of claim Eagle seeks to present does exist is a question for California law. The case should have been remanded to the

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[4]Before holding that it does not exist, it would be necessary to hold that Pacific had a claim against AT&T to which a stockholder's claim could be derivative. It would be necessary to hold that a corporation whose directors have pursued a course of conduct has a corporate claim for relief against the majority stockholder who selected those directors if the course of conduct turns out to be unwise, imprudent, and financially deleterious. That is a question of California law and could be decided by a federal court only if an action, in which *that* very contention of a derivative action *was asserted by the plaintiff*, was filed in a federal court or removed to it.

California courts to proceed as they, the sole interpreters of California law, should determine.

II.

THE COURT BELOW MISUSED PRETRIAL PROCEDURE TO ELIMINATE FROM CONSIDERATION A BASIS OF RECOVERY CLEARLY WITHIN THE PLEADINGS.

Having clung to jurisdiction, the District Court then dismissed the suit on motion for summary judgment. It reasoned that (a) if AT&T had allowed Pacific to do in the first place what the California Supreme Court held that it should have done — take accelerated depreciation with "flow-through" to the rate-payers — there would have been nothing to refund to rate-payers, and (b) that therefore the refund would leave Pacific where it would have been had AT&T allowed it to act properly in the first instance. Ergo, plaintiff suffered no damage. But the "ergo" requires a further supposition, that what plaintiff claims is a share of the refund. That reasoning founders on the fact that the claim for relief is not for a share of some "refund" but for damages sustained because an enormous and unnecessary tax liability was incurred which devalued plaintiff's shares of Pacific stock before plaintiff was forced to sell to AT&T on the merger. This is evident from the Amended Complaint (Appendix E), which contained these allegations (App. 25a, 26a):

> "6. American, as controlling stockholder of Pacific, elected all directors and, through the directors, elected all officers and made the policy decisions of Pacific, and owed, along with the directors and officers whom it chose and controlled, a fiduciary duty to plaintiff and the class members. Among such decisions was the deliberate choice to forego and not to claim deductions against federal income taxes of amounts for accelerated depreciation and investment tax credits, which decisions and choices were made for the benefit and enrichment of American, although injurious to the minority shareholders of Pacific, in violation of the

fiduciary obligation owed by defendant, as majority shareholder, to plaintiff and the class members.

"7. By reason of the actions referred to in the preceding paragraph, . . . Pacific was required . . . to refund $381,000,000 plus interest.

"8. By reason of the foregoing and as a proximate result thereof, defendant has caused the value of the shares owned by plaintiff and the class he represents to be reduced in the approximate amount of three dollars ($3.00) per share, resulting in damage to plaintiff in the approximate amount of $4,200 and damage to the class members collectively in an amount in excess of $38,000,000."

The prayer of the amended complaint was "For damages according to proof" (App. 27a).

Nothing in the pleading confined recovery to some share in a refund or precluded recovery of damages resulting from rejection of the opportunity to reduce taxes and consequent devaluation of plaintiff's shares. The opinion of the district court notes (at App. p. 18a) that in a "status conference order" further amendment of the pleading was precluded without permission, but no amendment would have been necessary to permit recovery on the basis of damages from the tax situation. Even before the teaching this Court had to administer to lower federal courts in *Conley v. Gibson*, 355 U.S. 41 (1957), that would have been obvious. It there said (pp. 47, 48):

> "all the Rules require is 'a short and plain statement of the claim' that will give the defendant fair notice of what the plaintiff's claim is and the grounds upon which it rests. * * * the simple guide of Rule 8(f) that 'all pleadings shall be so construed as to do substantial justice,' . . . . The Federal Rules reject the approach that pleading is a game of skill in which one misstep by counsel may be decisive to the outcome and accept the principle that the purpose of pleading is to facilitate a proper decision on the merits."

Except for purposes of relief in a default case a prayer is no part of a complaint; an action cannot be dismissed because a defendant is

not liable on the theory alleged in a complaint if the plaintiff is entitled to relief under the facts under any theory, asserted or not. Wright, Miller & Kane, *Federal Practice and Procedure,* § 2664, pp. 146, *et seq.* (2d ed. 1983). Judge Charles E. Clark, father of the Federal Rules, stated in *Gins v. Mauser Plumbing Supply Co.,* 148 F.2d 974, 976 (2 Cir. 1945), with concurrence of Judges Learned Hand and Augustus Hand, "the demand for judgment loses its restrictive nature when the parties are at issue, . . . particular legal theories of counsel yield to the court's duty to grant the relief to which the prevailing party is entitled, whether demanded or not."

None of these elementary principles of practice can be contested, and we doubt that they will be. Nothing was needed to expand the reach of plaintiff's claim. On the contrary, to support the judgment of dismissal, something was needed to *constrict* the relief. The courts below based such a constriction on pretrial occurrences. A "status conference order"(Appendix D, App. pp. 22a, 23a) recited that at a status conference the parties had proposed that "some or all of the legal issues presented by this complaint should be addressed by motions for summary judgment before proceeding with other aspects of the litigation including but not limited to the issue of class certification". The order then directed parties to "prepare a joint statement of undisputed facts that will serve as the foundation for cross motions for summary judgment". *But nothing in that or any other pretrial order purported to state, limit or constrict any legal theory.* In the subsequent 17 page stipulation of *facts,* after describing the refund of $418 million, a single sentence (on p. 16) stated: "it is this $418 million refund that forms the basis of plaintiff's complaint in this case". The totality of what the court added to this is (App. p. 19a) that in the subsequent memorandum of plaintiff in support of his motion for summary judgment against defendant, which was denied, his counsel stated that

> "The tax forgiveness added far more to the Pacific net worth than the refund had reduced it, but this action has been brought to recover only the damages suffered by the minority shareholders through the $417.1 million refund."

There is no reference to anything in plaintiff's memorandum in opposition to defendant's motion for summary judgment, which was the motion granted. None of this constituted an order constricting the issues.

The quoted phrasing of the claim by plaintiff's counsel in the District Court cannot be construed as stating that the relief sought was for a share of the refund and not for damages from the tax liability. If no refund had been ordered, no damage would have flowed from the higher tax which would have been absorbed by the rates. Counsel's phrasing did not lift the refund out of context of the tax liability. But this Court need not involve itself in interpreting statements of counsel who appeared for plaintiff in the district court. If counsel used inept phraseology, his ineptness cannot control disposition of the case and screen AT&T's conduct from judicial investigation to determine whether a huge corporate fiduciary is liable for inflicting millions in damages on minority shareholders of a subsidiary.

What we submit as so important as to call for this Court's attention is the use of pretrial procedure to work a throwback to antediluvian notions of "theory of the case". Pretrial orders and procedure under F.R.Civ.P. Rule 16 are of great worth in the administration of justice. They can serve to bring *facts* into focus, eliminate false claims of *fact*, and work simplification by taking advantage of undisputed *facts*. A party should be bound by admissions or statements of *fact* given at pretrial, and a pretrial order excluding an issue as "factually baseless" may well govern because it is a *factual* determination. (Cf. *Hale v. Firestone Tire & Rubber Co.*, 756 F.2d 1322, 1335 (8 Cir. 1985). F.R.Civ.P. Rule 16 provides for pretrial orders defining issues, but, consistent with the principles governing pleadings, such an order must "be liberally construed to embrace all of the legal and factual theories *inherent* in the issues defined therein", *Stone v. First Wyoming Bank N.A., Lusk*, 625 F.2d 332, 347 (10 Cir. 1980) (italics in original).

A fortiori, where there is no pretrial order defining issues, statements of counsel about a "theory" should not bar relief supported by the facts. Here, the pretrial order did not purport to limit or exclude any theory. Nor did the courts below base any

part of their decision on anything either in the pretrial order or in the pretrial proceedings about *facts*. They relied solely on statements by counsel, described above, to save them from considering relief which the facts and the pleadings permit.

Possibly a pretrial order which purports to limit issues *of law* might make it improper to grant a summary judgment *against* a defendant on a different claim. That is *United States v. First Nat. Bank of Circle*, 652 F.2d 882 (9 Cir. 1981), the principal reliance of the courts below; the theory of *Circle* was that ignoring a pretrial order would "bring back the days of trial by ambush and discourage timely preparation by the parties for trial" (p. 886). But that is the reverse of granting a summary judgment dismissing a plaintiff's case when the facts would warrant a recovery. Denying AT&T's motion for summary judgment would not ambush it or discourage timely preparation. Concurrently with the sentence from the stipulation of facts and the memorandum in support of his own motion referred to above, plaintiff's counsel was urging right of recovery on the theory of impairment of value of the stock.

Our submission is that the court below abused Rule 16 procedure, just as over 30 years ago courts abused pleading procedure until corrected by *Conley v. Gibson, supra*. It is now timely to remind lower federal courts that cases are not to be decided on the basis of how claims are formulated by a counsel's words and that they are to be determined on the basis of the fundamental grievance involved.

CONCLUSION

We respectfully submit that a writ of certiorari should issue.

Dated: San Francisco, California, January 27, 1986.

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Alexander F. Eagle

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APPENDIX A

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

CA No. 84-1636
DC No. 81-4078

OPINION

ALEXANDER F. EAGLE,
Plaintiff-Appellant,

vs.

AMERICAN TELEPHONE AND TELEGRAPH COMPANY,
a corporation,
Defendant-Appellee.

Appeal from the United States District Court
for the Northern District of California
Honorable William Schwarzer, District Judge, Presiding
Argued and Submitted December 13, 1984 —
San Francisco, CA
Filed: August 19, 1985

Before: CHOY, CANBY and NORRIS, Circuit Judges.

CANBY, Circuit Judge:

Pacific Telephone and Telegraph was ordered to refund $381 million in rate overcharges in 1980. That refund precipitated this lawsuit. Alexander F. Eagle filed a class action on behalf of Pacific's minority shareholders against Pacific's majority shareholder American Telephone and Telegraph (ATT), alleging that ATT breached its fiduciary duty owed to the minority shareholders. After the complaint was filed, ATT purchased the plaintiffs' shares in the merger of Pacific into ATT. The case was removed from state court to the District Court for the Northern District of California, which granted judgment in favor of ATT. At issue on appeal are (1) whether the case was properly removed from state court; (2) whether, assuming jurisdiction, the $381 million refund injured the minority shareholders; and (3) whether a pretrial order precluded Eagle from alleging a new claim at the summary judgment stage.

We affirm. We conclude that this class action was properly removed from state court because the federal court had original diversity jurisdiction. The minority shareholders' claims can be aggregated to satisfy the jurisdictional amount because the shareholders' claims derive entirely from an alleged injury to the corporation. We affirm the district court's finding that Eagle and other minority shareholders were not damaged by the refund. We also hold that the district court did not abuse its discretion in enforcing the pretrial order.

BACKGROUND

The minority shareholders seek relief for two alleged injuries. First, in 1980, the California Public Utilities Commission (CPUC) ordered Pacific to refund $381 million in rate overcharges to its ratepayers. Second, by 1981, Pacific had incurred a $1.5 billion tax liability that was on its books at the time of the ATT-Pacific merger. The minority shareholders contend that the refund and tax liability injured them by depressing the value of their Pacific stock.

The shareholders' allegations can only be understood in the context of a dispute in regulatory philosophy at the root of the refund and tax liability. In 1954, Congress enacted the accelerated depreciation tax provisions. A dispute arose over the appropriate treatment of accelerated depreciation for utility ratemaking. ATT and its subsidiaries advocated the use of normalization accounting. Under this method, the utility takes accelerated depreciation deductions and investment tax credits on its tax returns but only takes straight-line depreciation on its accounts used for ratemaking. The increment of actual tax savings above the straight-line deduction reflected in the ratemaking account is placed in a reserve account that generates income for investment in the utility plant. This method of treatment is supported as being in accord with the intent of Congress in allowing accelerated depreciation; it makes the tax savings available for investment in plant and equipment.

Some state regulatory commissions, however, adopted the view that any tax savings resulting from accelerated depreciation

should inure immediately to the benefit of the ratepayers. California was one of them, during much of the period relevant to this litigation. CPUC consequently took the position in 1960 that if a utility elected to use accelerated depreciation, then it must use a "flow-through" method of accounting for ratemaking purposes, which has the effect of passing the tax savings directly on to ratepayers.

The sparring among Congress, CPUC and similar state regulatory commissions, and Telephone companies like Pacific took a number of twists and turns. At the risk of oversimplification, only a few of them will be related here. Pacific initially refused to use accelerated depreciation (thereby losing some tax savings) because CPUC's policy would have required those savings to be passed on to ratepayers. (Pacific also asserted other reasons for preferring straight-line depreciation.) CPUC responded by ruling that it would set rates based on accelerated depreciation whether or not the telephone company elected it (thereby virtually forcing such an election whenever the company was free to make it). Congress in 1969 rejoined the battle by passing 26 U.S.C. § 167(1), which precluded companies from taking accelerated depreciation if they were forced to pass the tax savings on to ratepayers. CPUC subsequently adopted a number of differing positions, some induced by state court decisions reversing its rulings. At one point it permitted Pacific to elect accelerated depreciation and to retain the tax savings, and at another it required a flow-through, even retroactively.

There were two results of this protracted skirmishing that are relevant to this lawsuit. In 1974, CPUC permitted Pacific to retain tax savings from accelerated depreciation but, after a reversal in state court, it retroactively required a flow-through. It accordingly ordered a refund to ratepayers of $381 million ($418 million with interest). Pacific's former minority shareholders seek relief for that refund, arguing that management could somehow have avoided the loss if it had adopted accelerated depreciation from the beginning.

A second result was that, because of CPUC's ultimate position that tax savings had to be passed through, Pacific became ineligible for accelerated depreciation tax treatment under 26

U.S.C. § 167(1). Accordingly, it accrued a federal tax liability of some $1.5 billion. That tax liability was *still on Pacific's books* when ATT, then a 90 percent shareholder of Pacific, proposed a stock-for-stock merger with Pacific in October of 1981.

In September 1981, Eagle had filed this class action in California state court on behalf of Pacific's minority shareholders similarly situated. The complaint alleged that ATT used its ability to control Pacific to its own advantage and to the minority shareholders' detriment. Specifically, the complaint alleged that ATT caused Pacific to forego taking accelerated depreciation and investment tax credits, that ATT's imprudent decision caused Pacific to refund $381 million in rate overcharges and that the refund injured the minority shareholders by approximately $38 million (ten percent of the total refund).

ATT removed the class action to federal court pursuant to 28 U.S.C. §§ 1332 and 1441. After unsuccessfully petitioning for remand to state court, Eagle filed an amended complaint. The allegations remained essentially the same. Eagle, however, amended the damage allegation to state that the refund caused approximately $3.00 per share depreciation in the value of each share owned by minority shareholders and that Eagle individually was damaged by approximately $4,200. The complaint also alleged that after the initial complaint was filed, ATT offered to purchase the minority shares at a depressed price without compensating the minority shareholders for the damage caused by the refund. Eagle then filed a second motion for remand to state court that was denied.

In the meantime, Pacific and ATT filed for approval of the proposed stock-for-stock merger. CPUC held hearings at which Eagle and other minority shareholders appeared and contested the fairness of the proposed terms to the minority shareholders. Eagle argued that the proposed price for minority shares was inadequate because it did not reflect "pending federal legislation, which if enacted, would relieve (Pacific) of a substantial recorded tax liability," the $1.5 billion tax liability. CPUC, however, found that the exchange offer was "fair and reasonable" and that the approval of the merger would not adversely affect the interests of minority shareholders.

After the merger was complete, Congress enacted the Surface Transportation Assistance Act of 1982, Pub. Law No. 97-4241, 96 Stat. 2097, which reduced the $1.5 billion tax liability to approximately $320 million. Eagle then attempted to bring the tax liability into the class action at the summary judgment stage. Eagle alleged that the $1.5 billion tax liability depressed the value of the Pacific's shares at the time of the merger and that ATT received a windfall from the tax relief after the merger was consummated.

On cross-motions for summary judgment, the district court ruled in favor of ATT. The court held that the $381 million refund did not damage the minority shareholders because if Pacific had adopted accelerated depreciation in 1968, Pacific would not have collected an offsetting amount in rates. The court also held that a pretrial order precluded Eagle from asserting for the first time at the summary judgment stage that the tax liability depressed the exchange price he received for Pacific's shares in the ATT-Pacific merger. Alternatively, the court held that Eagle was collaterally estopped from making this claim by the CPUC finding that the exchange offer was fair to minority shareholders despite the possible tax forgiveness.

DISCUSSION

1. Jurisdiction

Eagle contends that this class action[1] was improperly removed from state court because Eagle's claim and the claims of some of the other shareholders that he represents do not satisfy the jurisdictional amount. The district court has original diversity jurisdiction in all civil matters where the parties are of diverse citizenship and the matter in controversy exceeds $10,000. 28 U.S.C. § 1332. The diversity of citizenship is not in issue. Jurisdiction in this case depends on the application of the aggregation

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[1]Even though no class certification has yet been sought, we assume for purposes of determining whether the district court had jurisdiction that this suit is a class action. *City of Inglewood v. City of Los Angeles*, 451 F.2d 948, 951 (9th Cir. 1971).

rules used to determine the amount in controversy. The individual claims of the minority shareholders' can be aggregated if they share a common and undivided claim. If, however, their claims are separate and distinct, aggregation is not permitted and each plaintiff must exceed the $10,000 statutory minimum to maintain diversity jurisdiction. *Snyder v. Harris*, 394 U.S. 332 (1969). Because we view the claims as common and undivided, we hold that the amount in controversy is the aggregated claims of the plaintiffs or $38 million and that the jurisdictional amount is satisfied. Thus, removal to the district court was proper.

Our starting point for determining the amount in controversy is to characterize the shareholders' claims under California state law. *Horton v. Liberty Mutual Insurance Co.*, 367 U.S. 348, 352-53 (1961). We confine our analysis to the claim as presented in Eagle's initial complaint because the amount in controversy is determined from the pleadings as they exist at the time a petition for removal is filed. *Pullman Co. v. Jenkins*, 305 U.S. 534, 537 (1939). *St. Paul Mercury Indemnity Co. v. Red Cab Co.*, 303 U.S. 283, 292 (1938).

Eagle's initial complaint asserts a cause of action for breach of the majority shareholder's fiduciary duty to minority shareholders. Under California law, the majority shareholder breaches his fiduciary duty if he uses his ability to control a corporation to his own benefit and to the detriment of the minority shareholders. *Smith v. Tele.-Communication, Inc.*, 134 Cal. App. 3d 338, 343, 184 Cal. Rptr. 571, 574 (1982); *Jones v. H.F. Ahmanson & Co.*, 1 Cal. 3d 93, 100, 81 Cal. Rptr. 592, 599, 460 P.2d 464, 471 (1969); 12B *Fletcher Cyclopedia Of The Law Of Private Corporations*, § 5811 (1984). Eagle's complaint alleges: that ATT, Pacific's majority shareholder, used its control of Pacific to elect directors that implemented ATT policy; that ATT policy caused Pacific imprudently to forego adopting accelerated depreciation and investment tax credits before the 1968 cutoff date; that this imprudent policy resulted in Pacific's being ordered to refund $381 million in rate overcharges; and that "the refund reduced or will reduce the assets of Pacific and the amounts otherwise available to pay as dividends to shareholders or to enhance the net worth of the underlying value of the shares owned by plaintiff and

the class he represents." The complaint prays for compensatory damages of at least $38 million and punitive damages of $20 million.

Normally, a shareholder cannot maintain an action in his individual capacity against a majority shareholder for the depreciation in the value of his stock resulting from a depletion of corporate assets because the depletion of corporate assets is a direct injury to the corporation and only an incidental injury to its shareholders. *O'Hare v. Marine Electric Co.*, 299 Cal. App. 2d 33, 39 Cal. Rptr. 799, 800 (1964); 12B *Fletcher Cyclopedia Of The Law Of Private Corporations* § 5812 at 173 (1984). The majority shareholder's duty must be enforced either directly by the corporation or through a shareholders' derivative suit.[2] Eagle and the class that he represents, however, no longer own Pacific stock because of the ATT-Pacific merger and therefore cannot bring a derivative shareholders' suit on Pacific's behalf against ATT. Cal. Corp. Code § 800(b). *See Watson v. Button*, 235 F.2d 235, 236-37 (9th Cir. (1956). Because Pacific's recovery for its alleged injury would not compensate the former minority shareholders for any loss they may have suffered as a result of the injury to Pacific, we are willing to assume that California would permit Pacific's former minority shareholders to bring this class action in their individual capacities.

We must now determine whether the minority shareholders' claims are separate and distinct or common and undivided within the meaning of the aggregation rules of *Snyder v. Harris*, 394

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[2]We note that Eagle's complaint prays for $38 million in damages or ten percent of the refund alleged to have injured Pacific. The class Eagle purports to represent owned approximately ten percent of Pacific's stock when the complaint was filed. Individual shareholder suits are not usually permitted when the shareholders share a common injury to their stock. 12B *Fletcher Cyclopedia Of The Law Of Private Corporatins* § 5913 (1984). Eagle's prayer for relief indicates that all of Pacific's shareholders suffered a common injury, divisible in proportion to their ownership of Pacific stock.

U.S. 332 (1969).[3] The dividing line is not clear. 14A C. Wright, A. Miller, E. Cooper, *Federal Practice And Procedure* § 3704 (1985). Eagle contends that the shareholders' claims are separate and distinct because under California law the minority shareholders each have an individual cause of action even though they were injured by a single wrongful act. ATT, however, contends that the claims are common and undivided because the shareholders' claims derive from their common and undivided interest in Pacific's assets.

We have previously held that the character of the interest asserted depends on the source of plaintiffs' claims. If the claims are derived from rights that they hold in group status, then the claims are common and undivided. If not, the claims are separate and distinct. *Potrero Hill Community Action Committee v. Housing Authority*, 410 F.2d 974, 978 (9th Cir. 1969). In *Potrero*, we held that the claims of tenants in a housing project were separate because their claims were derived from their own individual leases, not from rights that they held as a tenants' group. *Id.* Other courts have applied a property-based analysis to hold that plaintiffs making claims in their status as joint or co-tenants or under a single instrument share common claims. *See, e.g., Broenen v. Beaunit Corp.*, 305 F. Supp. 688, 692 (E.D. Wisc. 1969) (action to enforce terms of trust indenture is a true class action), *aff'd*, 440 F.2d 1244 (7th Cir. 1970); *Edgerton v. Armour & Co.*, 94 F. Supp. 549, 553-54 (S.D. Cal. 1950) (action for an accounting is a true class action because right asserted under a single contract); *See* 14B C. Wright, A. Miller, E. Cooper, *Federal Practice And Procedure* § 3704 at 483-85 (1985) for more examples of common and undivided claims.

These cases suggest that the shareholders' claims here are common and undivided. Under California law, the source of the

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[3]In *Snyder*, the Supreme Court preserved the character of interest analysis developed before the 1966 revision of Rule 23 of the Federal Rules of Civil Procedure to distinguish between spurious and true class actions. Claims of individual class members could only be aggregated in true class actions. 14B C. Wright, A. Miller, E. Cooper, *Federal Practice And Procedure* § 3705 (1985).

shareholders' claim for the wrongful depletion of corporate assets is the common and undivided interest each shareholder has in a corporation's assets and a right to share in dividends. *Miller v. McColgan,* 17 C.2d 432, 110 P.2d 419, 421 (1941). Because shareholders do not own the corporation's assets, the wrongful depletion of corporate assets is an injury to the corporation and only an indirect injury to the shareholders. For this reason, shareholders normally cannot recover in their individual capacities for a wrongful depletion of corporate assets. *O'Hare v. Marine Electric Co.,* 229 Cal. App. 2d 33, 39 Cal. Rptr. 799, 800 (1964).

It is true that we have assumed that California would permit the shareholders to sue individually in the circumstances of this case, in order to avoid the possibility of a wrong without a remedy. That permission, however, does not change the nature or source of the shareholders' claim, which is rooted in an injury to the assets of the corporation. The effect on the shareholders' stock value was indirect — a mere reflection of the alleged loss of corporate assets.

Insofar as the nature or source of their injury is concerned, the shareholders here are in the same position as shareholders bringing the more typical shareholders' derivative suit. Claims are aggregated in those cases because they are "favored with the fiction that plaintiffs' possible recovery is not the measure of the amount involved for jurisdictional purposes but that the test is the damage asserted to have been sustained by the defendant corporation." *Koster v. Lumbermens Mutual Casualty Co.,* 330 U.S. 518, 523 (1947), 14B C. Wright, A. Miller, E. Cooper, *Federal Practice And Procedure* § 3705 at 95 (1985).

The Supreme Court's decision in *Snyder v. Harris,* 394 U.S. 332 (1969), involved a different kind of claim. There minority shareholders brought a class action to recover the premium that certain majority shareholders received for the sale of their controlling stock. The Supreme Court did not permit aggregation. Under the applicable Missouri law, however, the minority shareholders had an individual and direct right to recover a share of the premium received by the majority controlling shareholders. No right accrued to the corporation and no injury was done to the corporation. The claim of the minority shareholders was in no way

dependent upon or derivative of an injury to the corporation. Quite the contrary is true of Eagle's claim, which derives wholly from an alleged injury to the corporation's assets.[4]

We conclude, therefore, that the minority shareholders' claims asserted in this case must be characterized as common and undivided. Therefore, the amount in controversy is the $38 million fund that Eagle sought in his initial complaint. The district court properly exercised jurisdiction after removal of this case from state court pursuant to 28 U.S.C. §§ 1332, 1441 because the district court had original diversity jurisdiction.

2. Standard of Review

We review a grant of summary judgment de novo to determine whether there is a genuine issue of material fact and whether the substantive law was correctly applied. *Greenfield v. Kootenai County*, 752 F.2d 1387, 1388 (9th Cir. 1985). The material facts are set forth in two stipulations of fact filed by the parties and are not in dispute.[5]

3. Damages Caused by the Refund

Eagle contends that the $381 million refund injured the minority shareholders by depreciating the value of their stock. The district court held that the refund did not injure the minority shareholders because if Pacific had avoided the refund by adopting accelerated depreciation, the tax benefit would have flowed through to the ratepayers and Pacific would not have collected an offsetting amount in utility rates. We agree with the district court that the minority shareholders were not injured by the $381

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[4]The shareholders intended division of the $38 million fund pro rata does not make their claims separate and distinct. It is proper to aggregate the value of jointly held rights when "several plaintiffs sue to enforce a common and undivided interest which is separate and distinct as between themselves." 1 *Moore's Federal Practice* § 0.97[3] at 962 (1984).

[5]We reject Eagle's argument in his brief that there is a material issue of fact for trial on whether Eagle was damaged.

million refund.[6] The district court properly entered summary judgment in favor of ATT on Eagle's refund claim because a plaintiff cannot state a claim in the absence of an injury.

4. Pretrial Order

At the oral argument on the cross-motions for summary judgment, Eagle attempted to articulate a new damage theory; namely, that the minority shareholders' shares were undervalued at the time of the ATT-Pacific merger because of a $1.5 billion tax liability then on Pacific's books that was reduced after the merger was completed. Eagle contended that the tax liability would not have accrued if Pacific had adopted accelerated depreciation in 1968[7]. Eagle did not change its prayer for damages; it continued to request $38 million or ten percent of the refund (approximately $42 million with interest). The district court held that new theory was precluded by a pretrial Status Conference Order issued on January 10, 1983, pursuant to the parties' stipulation.

On appeal, Eagle contends that under Rule 54(c) of the Federal Rules of Civil Procedure he is entitled to the appropriate relief for his claim based on breach of fiduciary duty even if he has not demanded that relief in his pleadings. He argues that the short and plain statement of his claim in his complaint encompassed his new theory of damages and that the district court incorrectly characterized this theory as a new claim.

We agree with the district court that the pretrial Status Conference Order precluded Eagle from raising a new theory of relief at the summary judgment stage. The order provided that "[n]o further motions for leave to amend the complaint will be entertained except on showing of good cause based on new facts that have come into existence subsequent to the date of this

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[6]We note that Eagle virtually abandoned this theory of liability on appeal in favor of his theory that the tax liability injured the minority shareholders.

[7]Of course, CPUC would presumably have required much or all of the saving to be passed on to ratepayers.

order." A Rule 16(e) order controls the subsequent course of action in the litigation unless it is modified by a subsequent order. Fed. R. Civ. P. 16(e). Although we liberally construe pretrial orders, a theory will be barred if not at least implicitly included in the order. *United States v. First National Bank of Circle*, 652 F.2d 882, 886 (9th Cir. 1981).

We find that the tax liability theory was not implicit in the pretrial order. Eagle's initial and amended complaints allege that the minority shareholders were injured by the refund Pacific was ordered to pay. Neither complaint mentions the tax liability. The Stipulation of Facts filed by both parties pursuant to the Status Conference Order states that "[i]t is this $418 refund [$381 refund with interest] that forms the basis of plaintiff's complaint in this case." Until the summary judgment stage, Eagle framed his claim as a right to recover for the portion of the refund. Only then did he attempt to change his theory of recovery. It would be unfair to the defendant to permit the plaintiff to change strategies at that late stage of litigation. The district court did not abuse it discretion by enforcing the pretrial order.

Because we uphold the enforcement of the pretrial order, we do not reach the issue of whether the CPUC decision approving the ATT-Pacific merger collaterally estopped Eagle from raising the tax liability theory.

AFFIRMED.

APPENDIX B

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

CA No. 84-1636

ORDER

ALEXANDER F. EAGLE,
Plaintiff-Appellant,

vs.

AMERICAN TELEPHONE & TELEGRAPH COMPANY,
Defendant-Appellee.

Filed: October 30, 1985

Before: CHOY, CANBY and NORRIS, Circuit Judges.

The panel has voted unanimously to deny the petition for rehearing and suggestion for rehearing en banc.

The full court has been advised of the suggestion for rehearing en banc and no judge of the court has requested a vote to rehear the matter en banc.

The petition for rehearing is hereby denied and the suggestion for rehearing en banc is rejected.

APPENDIX C

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

No. C-81-4078-WWS

MEMORANDUM OF OPINION AND ORDER

ALEXANDER F. EAGLE,
Plaintiff,

vs.

AMERICAN TELEPHONE & TELEGRAPH COMPANY,
a corporation,
Defendant.

Filed: , 1985

This action is before the Court on cross-motions for summary judgment. The parties have filed stipulations setting forth the material facts, none of which are in dispute.

FACTUAL BACKGROUND

Plaintiff is a former minority shareholder of what was the Pacific Telephone & Telegraph Company ("Pacific"). He sues on behalf of a purported class of minority shareholders whose shares were acquired about October 1981 through a merger with what was American Telephone & Telegraph Company ("AT&T"), then the owner of approximately 90 percent of the common shares of Pacific.

In his amended complaint, plaintiff alleges that AT&T abused its fiduciary duties as a majority shareholder by causing Pacific not to claim federal tax deductions for accelerated depreciation and investment credits, resulting in an order requiring Pacific to refund some $381 million plus interest to ratepayers. As a consequence, the value of each share held by minority shareholders was reduced by about $3.00. The complaint seeks compensatory damages accordingly as well as punitive damages.

Pursuant to stipulation of the parties, the Court on January 10, 1983, entered an order submitted by the parties providing that the

parties would prepare and submit a joint statement of undisputed facts as a foundation for cross motions for summary judgment. That has been done and the material facts are set forth in two stipulations of facts, which may be summarized as follows:

Beginning in 1960, the California Public Utilities Commission ("CPUC") took the position that California public utilities would not be required to claim accelerated depreciation on their federal income tax, but if they did, the tax savings would be "flowed through" to ratepayers. Pacific opposed flow-through and accordingly declined to claim accelerated depreciation deductions, adhering instead to the straight-line method of depreciation accounting. In 1968, the CPUC changed its position and required utilities to claim accelerated depreciation and flow through the benefits to ratepayers by setting rates on a basis reflecting accelerated depreciation deductions regardless of whether the utility actually claimed accelerated depreciation. Pacific still declined to claim accelerated depreciation.

In 1969, Congress adopted the Tax Reform Act of 1969, which required utilities that had not theretofore claimed accelerated depreciation but wished to claim it in the future to account for the tax benefits on a "normalized" rather than flow-through basis.[1] CPUC, in response to the Act, allowed Pacific in 1970 to claim accelerated depreciation without flow-through; Pacific claimed accelerated depreciation that year for the first time. In 1971, however, the Supreme Court of California vacated the CPUC order. The Court held that Pacific had been "imprudent" in not claiming accelerated depreciation in 1968 (when the tax savings would, under the CPUC order then in force, have flowed through to ratepayers), which had rendered it ineligible under the Tax Reform act to claim accelerated depreciation with flow-through under the 1969 Act. The Court remanded the matter to the

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[1]In the Revenue Act of 1971, Congress authorized investment tax credits for utilities such as Pacific on terms identical to those it had attached to accelerated depreciation in 1969. Congress, Pacific, CPUC, the California Supreme Court and the IRS have at all relevant times treated these tax benefits identically for ratemaking and income tax purposes.

CPUC to consider setting rates on the basis of "imputed flow-through," that is, to set rates passing the benefits of accelerated depreciation deductions on to ratepayers regardless of the fact that Pacific would not be eligible to claim them.

In 1972, CPUC ordered Pacific to refund overcharges resulting from the rates set during the 1970-72 period on a normalized basis (in conformity with the Tax Reform Act). This refund is not at issue in this action. In 1974, however, CPUC again authorized rates on a normalized basis, having considered and rejected the option of imputed flow-through. The rates were set on this basis subject to refund should the California Supreme Court again find the rate order objectionable. In 1975 the Supreme Court again vacated the order on the ground that the CPUC had failed to consider alternatives to strict normalization.

In 1977, the CPUC adopted a modified normalization method that flowed through some of the tax savings from accelerated depreciation and investment tax credits. It ordered a refund of overcharges (the difference between the normalized and modified normalized rates) during the period 1974-77. This order was stayed pending appeal.

In 1978, Pacific secured a ruling from the Internal Revenue Service that the modified normalization method imposed by the CPUC did not qualify Pacific to claim accelerated depreciation under the 1969 Act or investment tax credits under the 1971 Act. The result of this ruling was to leave Pacific not only subject to the refund order but also ineligible for the tax savings on which the modified flow-through rates set by the CPUC were premised. As a result, Pacific incurred and carried on its books a liability for taxes, which ultimately rose to about $1.5 billion, created by its ineligibility for accelerated depreciation and investment tax credits.

The appeals from the CPUC order of 1977 imposing modified normalization were exhausted in 1980. At that time, Pacific became obligated to refund the overcharges it had collected for the 1974-80 period based upon its normalized rates, plus interest. It is this refund of about $418 million ($381 million plus interest) that is the subject of plaintiff's claim.

In 1981, AT&T proposed a stock-for-stock merger with Pacific. The merger required CPUC approval. Before the CPUC, plaintiff objected on a number of grounds, one of which being that the value established for Pacific's shares did not adequately reflect the prospect of future forgiveness of the large tax liability on Pacific's books on account of its failure to have taken accelerated depreciation. That prospect rested on legislation then pending in Congress to forgive that liability. In its order approving the merger over plaintiff's objection, the CPUC rejected the contention, finding that the price per share, which reflected book value after giving effect to the entire tax liability, was within the "range of reasonableness." The merger was then consummated on the approved terms.

In 1982, Congress adopted the Surface Transportation Assistance Act, which in fact forgave a large portion of the tax liability.

DISCUSSION

1. Plaintiff suffered no damage.

Plaintiff alleges that AT&T abused its fiduciary duties. He argues that because AT&T opposed flow-through ratemaking for its own benefit, it prevented Pacific from claiming accelerated depreciation, thereby eventually subjecting it to the $381 million refund order.

That claim is patently without merit. It is self-evident from the stipulated facts that plaintiff and his fellow minority shareholders, as well as Pacific, were in exactly the same position after the refund was ordered as they would have been in had Pacific claimed accelerated depreciation. In that event, the tax savings would have been required to flow through to the rate payers and the $381 million in rates required to be refunded *would never have been collected in the first place.* Plaintiff and the other minority shareholders therefore suffered no injury and hence defendant is entitled to summary judgment on the claim.

2. Plaintiff's New Claim Must be Rejected.
   a. Plaintiff's New Claim is Barred by the Court's Prior Order.

Plaintiff does not dispute the foregoing analysis. His response consists of raising an entirely new claim, namely that as a result of Pacific's refusal to claim accelerated depreciation, it incurred a $1.5 billion tax liability which reduced its balance sheet net worth, and hence the value of the minority shares at the time of the merger. That claim must be rejected for several separate and independent reasons.

In paragraph 6 of his amended complaint filed January 5, 1982, plaintiff alleged that AT&T, as Pacific's controlling shareholder, caused it to make decisions for AT&T's benefit and injurious to Pacific's minority shareholders. The amended complaint then goes on to allege:

> 7. *By reason of the actions referred to in the preceding paragraph,* which actions have been declared by the California Public Utilities Commission to be imprudent management, Pacific was required by an order dated September 13, 1977, issued by said Commission to refund to its subscribers or ratepayers the sum of $205,586,000. Said order was confirmed by a further order of the California Public Utilities Commission dated February 13, 1980, which required Pacific to refund $381,000,000 plus interest.
>
> 8. *By reason of the foregoing and as a proximate result thereof,* defendant has caused the value of the shares owned by plaintiff and the class he represents to be reduced in the approximate amount of three dollars ($3.00) per share, resulting in damage to plaintiff in the approximate amount of $4,200 and damage to the class members collectively in an amount in excess of $38,000,000.
> (Emphasis added)

On January 10, 1983, this Court, pursuant to the parties' stipulation, entered an order stating in part that

> no further motions for leave to amend the complaint will be entertained except on showing of good cause based on new

> facts that have come into existence subsequent to the date of this order.

Thereafter in the stipulation of fact submitted pursuant to the Court's order, plaintiff stipulated that "[i]t is this $418 million refund [including the interest] that forms the basis of plaintiff's complaint in this case." (Ex. A, p. 16, lines 18-19).

And in his memorandum in support of his own motion for summary judgment filed as recently as October 31, 1983, plaintiff describes his claim as follows:

> The tax forgiveness added far more to the Pacific net worth than the refund had reduced it, *but this action has been brought to recover only the damages suffered by the minority shareholders through the $417.1 million refund.* (Memo p. 9, emphasis added)

Plaintiff now argues that paragraph 6 of his amended complaint is simply "the short and plain statement of the claim" called for by Fed. R. Civ. P. 8. He refers to the general allegations of breach of fiduciary duties in the complaint and concludes:

> The complaint meets the requirements of Rule 8, if paragraph 7 were disregarded.

The Court is not disposed to disregard paragraph 7 or plaintiff's other repeated representations to the Court concerning the specifics of his claim. We are at this stage of the case not concerned with such preliminary matters as the sufficiency of a pleading or the scope of discovery. Rather, the question is what issue is presented for decision by the Court. Plaintiff has repeatedly framed that issue as being the right of the minority shareholders to recover an allocable share of the refund. He consented to the entry of the pretrial order of January 10, 1983, barring further amendments of the pleadings. That order, read in conjunction with the amended complaint and the stipulation of fact, clearly precludes plaintiff from advancing a new claim never before explicated (one which would raise the amount in issue from $38 million to $150 million). *See United States v. First Nat'l Bank of Circle,* 652 F.2d 882, 886-87 (9th Cir. 1981).

b. Plaintiff's New Claim is Without Merit as a Matter of Law.

Inasmuch as plaintiff's latter-day claim for a share of the $1.5 billion tax liability is not discussed in any of the papers he has filed with the Court, its theoretical basis is not clear. On any theory, however, the claim is meritless.

If plaintiff's argument is that the minority shares were undervalued at the time of the merger because the prospect of legislation forgiving the tax liability on the books was not taken into account, that issue was squarely raised by plaintiff before the CPUC and rejected. In its order approving the merger, the CPUC, notwithstanding the possibility of forgiveness of the tax liability, specifically found that "the exchange offer is fair and reasonable" and that "the interests of minority shareholders will not be adversely affected by approval of the merger." (CPUC Decision 82-05-007, Def. Opp. Memo. Att. 1, p. 42). That decision is final and hence gives rise to collateral estoppel on this issue. *Waters v. Pacific Telephone Co.*, 12 Cal. 3d 1, 10-11 (1974); *People v. Western Air Lines, Inc.*, 42 Cal. 2d 621, 630 (1954).

That order precludes any claim against the majority shareholder based on a theory that it violated its fiduciary duties by keeping for itself the benefit of the tax refund rather than sharing it with the minority shareholders. That issue was necessarily decided when the CPUC approved the price in the face of plaintiff's argument that a tax refund was foreseeable.

If, on the other hand, plaintiff's claim is based on injury he suffered flowing from the injury to Pacific caused by AT&T's mismanagement which resulted in a large tax liability, that claim is barred as well. Claims for injury to a corporation belong to the corporation; they can be asserted by shareholders only as derivative claims. *See Sherman v. British Leyland Motors, Ltd.*, 601 F.2d 429, 440 n.13 (9th Cir. 1979); *Jones v. H.F. Ahmanson & Co.*, 1 Cal. 3d 93, 105-08 (1969). Plaintiff has not alleged a derivative claim or met the requirements of Fed. R. Civ. P. 23.1. On this ground, any claim based on losses suffered by Pacific, including the rate refund, are barred.

Accordingly, even if it were open to the Court to consider plaintiff's new claim on the merits, it would have to be rejected as a matter of law.

For the reasons stated, judgment will be entered for defendant, defendant to recover its costs.

IT IS SO ORDERED.

DATED: January 23, 1984

/s/ WILLIAM W. SCHWARZER
WILLIAM W. SCHWARZER
United States District Judge

APPENDIX D

United States District Court
for the
Northern District of California
No. C-81-4078 WWS
STATUS CONFERENCE ORDER
ALEXANDER F. EAGLE,
Plaintiff,
vs.
AMERICAN TELEPHONE & TELEGRAPH COMPANY,
a corporation,
Defendant.

Filed: January 10, 1983

Counsel for the parties having appeared at a status conference on January 7, 1983, at which they proposed that, if possible, some or all of the legal issues presented by this complaint should be addressed by motions for summary judgment before proceeding with other aspects of the litigation including but not limited to the issue of class certification; the parties having agreed to attempt to prepare a joint statement of undisputed facts that will serve as the foundation for such motions and that little or no discovery should be needed in support of their motions; and, plaintiff having represented that no further amendments of his complaint are necessary or will be sought, it is hereby ORDERED:

1. Plaintiff and defendant shall prepare a joint statement of undisputed facts that will serve as the foundation for cross motions for summary judgment. The joint statement will be completed on or before March 7, 1983.

2. A further status conference will be held on March 11, 1983, 10 A.M., at which the parties should be prepared to discuss whether either party will require discovery prior to the filing of motions for summary judgment, the schedule for such discovery, if any, and the schedule for the filing of motions for summary judgment.

3. No further motions for leave to amend the complaint will be entertained except on showing of good cause based on new

facts that have come into existence subsequent to the date of this order.

Dated: January 10, 1983.

/s/ WILLIAM W. SCHWARZER
WILLIAM W. SCHWARZER,
Judge of United States District Court

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APPENDIX E

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA
No. C-81-4078-WWS

MINORITY SHAREHOLDER'S AMENDED COMPLAINT FOR DAMAGES

[Class Action]

ALEXANDER F. EAGLE, individually and on behalf of all others similarly situated,
Plaintiff,
vs.
AMERICAN TELEPHONE & TELEGRAPH COMPANY, a corporation,
Defendant.
Filed: January 5, 1982

Plaintiff alleges:

1. Plaintiff Alexander F. Eagle is now and at all times herein mentioned was a resident of Sonoma County, California, and a shareholder owning 1400 shares of The Pacific Telephone & Telegraph Company, a corporation (hereafter Pacific).

2. Defendant American Telephone & Telegraph Company (hereafter American) is and at all times herein mentioned was a corporation duly organized and existing under the laws of the State of New York doing business in the State of California and having its principal place of business in California located in the City and County of San Francisco. Defendant is and at all times herein mentioned was the dominant shareholder of Pacific Telephone, being the owner of approximately 90 percent of the issued and outstanding shares of said corporation.

3. Plaintiff brings this action on his own behalf and on behalf of all other persons similarly situated. The class which plaintiff represents is composed of the minority shareholders of Pacific, i.e., all of the shareholders of said corporation other than defendant. The persons in the class are so numerous, consisting of several hundred individuals and entities, that the joinder of all such persons is impracticable. The disposition of their claims in a class action is a benefit to the parties and to the court.

4. There is a well-defined community interest in the questions of law and fact involved herein affecting the parties to be represented in that each and all of them have suffered damage in the same manner and by reason of the same unlawful conduct, varying only in the amounts of damage suffered by each, all resulting by reason of the actions and activities of defendant in controlling, managing, operating and using Pacific for defendant's advantage in violation of the rights of all minority shareholders. Proof of a common or single state of facts will establish the right of each member of the class to recover. The claims of the plaintiff are typical of those of the class and plaintiff will fairly and adequately represent the interests of the class.

5. There is no plain, speedy or adequate remedy other than by maintenance of this class action since plaintiff is informed and believes that the damage to most members of the class is relatively small in that most own only a few shares each, thus making it economically infeasible to pursue remedies other than a class action. Consequently, there will be a failure of justice but for the maintenance of the class action.

6. American, as controlling stockholder of Pacific, elected all directors and, through the directors, elected all officers and made the policy decisions of Pacific, and owed, along with the directors and officers whom it chose and controlled, a fiduciary duty to plaintiff and the class members. Among such decisions was the deliberate choice to forego and not to claim deductions against federal income taxes of amounts for accelerated depreciation and investment tax credits, which decisions and choices were made for the benefit and enrichment of American, although injurious to the minority shareholders of Pacific, in violation of the fiduciary obligation owed by defendant, as majority shareholder, to plaintiff and the class members.

7. By reason of the actions referred to in the preceding paragraph, which actions have been declared by the California Public Utilities Commission to be imprudent management, Pacific was required by an order dated September 13, 1977, issued by said Commission to refund to its subscribers or ratepayers the sum of $205,586,000. Said order was confirmed by a further order

of the California Public Utilities Commission dated February 13, 1980, which required Pacific to refund $381,000,000 plus interest.

8. By reason of the foregoing and as a proximate result thereof, defendant has caused the value of the shares owned by plaintiff and the class he represents to be reduced in the approximate amount of three dollars ($3.00) per share, resulting in damage to plaintiff in the approximate amount of $4,200 and damage to the class members collectively in an amount in excess of $38,000,000.

9. Plaintiff is informed and believes and therefore alleges that American has engaged in other activities of like nature, in breach of its fiduciary duty in controlling, managing, operating and using Pacific for its own advantage and profit and to the injury and damage of plaintiff and the class, the details of which are not now known to plaintiff, and plaintiff prays leave, when the same become known, to amend this complaint in order to set forth the facts thereof and to allege the damages to plaintiff and the class resulting therefrom. Such additional activities have also had the effect of reducing the value of shares owned by plaintiff and the class members.

10. In the activities of defendant alleged herein, defendant has intentionally violated a fiduciary relationship for its own gain and has acted to injure the minority shareholders in a wanton, malicious and oppressive manner in depriving them of their rights and diminishing the value of their shares. By reason thereof, plaintiff and the class are entitled to exemplary and punitive damages for the purpose of punishing defendant in the amount of two dollars per share, which, when multiplied, totals $2,800 for plaintiff and approximately $30,000,000 for the members of the class collectively.

11. Having caused the value of shares owned by minority shareholders to be reduced as aforesaid, defendant has, subsequent to the filing of the original complaint herein, offered to purchase the minority shares at the price of thirty-five one hundredths (.35) of one of defendant's own shares for each minority share, which amounts to about $20.69 per share, and has organized a wholly-owned subsidiary to effect such purchase and

is proceeding in an endeavor to compel minority shareholders to accept that depressed price, without compensating them for the damages complained of herein.

12. Plaintiff has incurred, and during the pendancy of this action, will incur expenses for attorney fees and costs herein. Such attorney fees and costs are necessary for the prosecution of the action and will result in the benefit to each of the members of the class. A reasonable attorney fee is a sum equal to 20 percent of the first two million dollars of recovery, 15 percent of the next 23 million dollars of recovery and 12½ percent of the excess over 25 million dollars of recovery.

WHEREFORE, plaintiff prays judgment as follows:

1. For damages according to proof, with interest thereon at the legal rate for each member of the class;

2. For exemplary and punitive damages in the sum of two dollars ($2.00) per share owned by each minority shareholder in the class.

3. For the payment of plaintiff's attorney fees out of the monies recovered for the benefit of the members of the class;

4. For costs of suit herein incurred; and

5. For such other and further relief as the court deems meet and just to the premises.

Dated: December 30, 1981.

ANGELL, HOLMES & LEA

By SAMUEL L. HOLMES
Attorneys for Plaintiff